

An item becomes realty after installation if it is physically affixed to the realty and the party affixing the item intends to make it a part of the realty.

May 31, 2001

Dear Xxxxx:

This will acknowledge receipt of your letter dated May 9, 2001. The nature of your letter and the information you have provided require that we respond with a General Information Letter, which is designed to provide general information, is not a statement of Department policy and is not binding on the Department. See 2 Ill. Adm. Code 1200.120 subsections (b) and (c), which can be found at <http://www.revenue.state.il.us/legalinformation/regs/part1200>.

In your letter, you have requested a determination that the material handling systems that are designed, manufactured and installed by your client constitute retail sales of tangible personal property subject to retailers' occupation tax liability. You have described the systems as follows:

"Our client designs and manufactures material handling systems for distribution, manufacturing, parcel and freight and baggage handling applications. Their systems include services that range from initial concept discussion with the client or their consultant through design, manufacture, installation, training, commissioning and ongoing support for their material handling systems. Their clientele cover various industries; therefore, their products must be flexible and allow for the combination of various components to create the most efficient system for each client application.

"Material handling systems are normally added after a building is completed and has already existed. The supporting components are normally bolted to the floors and ceilings and can be repaired or serviced while the system remains at its original location or is removed or replaced. Systems are intended to be flexible to allow for future expansions, variances in product sizes and types and changes for modernizing and updating of equipment.

"Our client's cost of machinery ranges from 55% to 70% of the total cost to design, manufacture and install the material handling system. Of the 55%-70% of machinery, approximately 57% is directly related to material costs for the conveyor belts. The remaining costs represent labor and overhead. Though each material handling system is customized to meet the needs of each individual facility, most conveyor systems contain the same base components and are similar to other systems manufactured by our client."

Based on the information contained in your letter, we are unable to determine whether the systems remain tangible personal property after installation or become affixed to the realty. However, based

on your description, we lean toward the conclusion that the systems remain tangible personal property.

For purposes of the Illinois sales tax laws, the Department uses an intention test to determine whether items remain tangible personal property after installation or become part of realty. If circumstances indicate that the parties obviously intended that the item remain with the realty, we give effect to that intention. If an obvious intent is not apparent, we look to the extent to which the item has been affixed. If the item can be removed without damage to the item or to the real estate, that is an indication that the parties intended that the item remain tangible personal property. We understand that your client's material handling systems can be removed without damage to the system components or to the real estate and that the systems are often moved within the buildings in which they are installed to accommodate expansions and updates to the systems. In addition, the Department looks to externals to determine intent. So, for example, if a contract for sale indicates that the seller can repossess the item in the event of non-payment, we think that is an indication that the parties intended that the item remain tangible personal property. (A seller of building materials that are incorporated into real estate can not repossess those materials but, instead, is limited to filing a mechanic's lien on the real estate.) We understand from our telephone conversation on May 31st that your client's sales contracts provide for repossession in the event of non-payment. Again, we think this is an indication that your client and its customers intend that the systems remain tangible personal property after installation.

From the information contained in your letter, we are unable to determine whether the sale and installation of the material handling systems constitute retail sale situations or service situations. If the systems are made up of standard components, a retail sale situation exists. On the other hand, if your client's customers come to your client primarily for its design expertise and if an individual system is so unique that it has value only to the customer for which it was designed, then a service situation exists. Your attention is directed to Velten & Pulver v. Department of Revenue, 29 Ill. 2d 524 (1963). In that case, the Illinois Supreme Court held that the design and fabrication of a specially designed bakery conveyor system constituted a service situation rather than a retail sale situation and, as a result, service occupation tax, rather than retailers' occupation tax, was due.

In a retail sale situation, retailers' occupation tax is due on the entire selling price of the item. See, 86 Ill. Adm. Code 130.100 et seq. In a service situation, service occupation tax is due on the separately stated selling price of the tangible personal property transferred incident to service (but not less than the serviceman's cost price of the items transferred.) This would be the case, for example, where a serviceman billed for the tangible personal property separate and apart from design services on invoices to service customers. If a serviceman does not show the tangible personal property as a separate item on invoices to service customers, then the service occupation tax is due on 50% of the serviceman's entire service billing (but not less than his cost of the items transferred). De minimus servicemen who are not otherwise required to register as Illinois retailers (servicemen whose cost price of tangible personal property transferred is less than 35% of their gross proceeds from sales of service and who do not otherwise make retail sales) do not incur service occupation tax liability. Rather, these de minimus servicemen incur a use tax liability based on their cost price of the items they transfer to service customers and their customers incur no tax liability. See 86 Ill. Adm. Code 140.101 et seq. Since your client's cost price of the materials that make up the material handling systems exceeds 35% of its gross receipts from sales, your client is not a de minimus serviceman.

If you would like a binding Private Letter Ruling regarding this matter and your client is not under audit, please submit all of the information set out in items 1 through 8 of 86 Ill. Adm. Code 1200.110(b).

Very truly yours,

George Sorensen  
Deputy General Counsel  
Sales and Excise Taxes